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December 22, 1994

Ms. Rosalind K. Allen  
Acting Chief  
Commercial Radio Division  
Wireless Telecommunications Bureau  
Federal Communications Commission  
2025 M Street, N.W. -- Room 5202  
Washington, D.C. 20554

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JAN 27 1995

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY

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Re: PP Docket No. 93-253: Implementation  
of Section 309(j)

Dear Ms. Allen:

We are writing to request clarification with respect to three questions concerning our interpretation of the recent Fifth Memorandum Opinion and Order in the above-referenced docket, involving the control group requirements for an applicant seeking to qualify as a small business owned and controlled by women and/or minorities ("PCS Co."). We also request clarification with respect to our understanding of the Commission's policy with respect to pledges of stock to lenders and equipment vendors.

At present, the control group of PCS Co. consists of the following elements:

° Company A: a pre-existing enterprise qualified for 8(a) status under the Small Business Administration Act. Company A is controlled by Investor A, a U.S. citizen who is a member of a minority group. Investor A is the President of Company A, a full time managerial position. Investor A owns 60 percent of its voting stock, and over 80 percent of its equity; some of the remaining voting stock and equity in Company A are held by non-qualifying investors. PCS Co. intends to enter into an agreement with Company A whereby Company A will provide the following services to PCS Co.: engineering and engineering

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support, project management, network planning, negotiation, personnel support, and administrative support.

- Investor B: a female U.S. citizen who is also an officer with managerial responsibility in PCS Co., but not the CEO or President of the applicant.

- Investor C: a white male who is the husband of Investor B and President and CEO of PCS Co.

- Together, Company A and Investor B will own over 50 percent of the voting stock in PCS Co. and over 15 percent of its equity.

\* \* \*

We request your confirmation of our understanding of the Commission's rules in the following areas.

1. Pre-Existing Entities Controlled by Minorities and/or Women Qualify As Minorities and/or Women For Purposes of Determining Whether An Applicant Satisfies the Control Group's Minimum Voting Stock Requirement. The Fifth Memorandum granted additional flexibility to applicants by allowing entities that are controlled -- but not 100 percent owned -- by minorities, such as Company A, to be part of the control group. See Fifth Memorandum Opinion and Order, PP Docket No. 93-253, ¶ 62 (hereinafter, Fifth Memorandum). Although the rules are clear that the Commission will use a multiplier rule to calculate whether entities controlled, but not 100 percent owned, by minority investors meet the minimum equity requirements announced in the Commission's rules, we request confirmation that the rules do not require a multiplier rule for purposes of determining whether an entity such as Company A meets the minimum 50.1 percent voting stock requirement.

We believe this was clearly the Commission's intent. In requiring use of the multiplier developed in the context of the broadcast multiple ownership rules, while not adopting the 51% control exception used there, the Commission stated that "we are using a multiplier only to determine a control group member's equity investment, not whether such a member has control or substantial influence over the applicant." Fifth Memorandum ¶ 71 n.170 (emphasis added). In the broadcast context, where voting power is the relevant question, the Commission has recognized that it is inappropriate to use a multiplier to measure the

voting power of those in voting control. 47 C.F.R. § 73.3555 note 2(d). Instead, it has taken a "pass through" approach, which appropriately "reflects the line of de jure control." Attribution of Ownership Interests, 97 F.C.C.2d 997, 1018 (1984).

Similarly, treating Company A as minority for purposes of satisfying the 50.1 percent minimum voting stock requirement is consistent with the Commission's concern that minorities and women effectively exercise ownership and control over applicants that seek benefits accorded to designated entities. This is because the non-controlling voting interests of non-qualifying investors in Company A do not dilute the ability of Investor A to control Company A. In other words, the non-controlling investors do not control or have the power to control Company A. --See, e.g., Fifth Report and Order, PP Docket No. 93-253 ¶¶ 204-206 (hereinafter the Fifth Report and Order) (discussing general principles of affiliation). Because minority Investor A controls Company A, he controls its actions as a member of the control group of PCS Co. As noted above, we recognize that non-controlling investors in the control group have the ability to dilute the amount of equity held by qualifying investors in PCS Co. and therefore understand the need for a multiplier rule in that context.

2. De Facto Control Requirements May be Satisfied Upon Showing That Managerial Positions Are Held By Qualifying Investors in The Control Group And Non-Controlling Investors in Entities That Are Part of The Control Group. The Commission's rules are designed to encourage participation in the PCS auctions by small businesses. However, the regulations implementing Section 8(a) of the Small Business Act require a "socially disadvantaged" person to serve as the President or Chief Executive Officer of a small business and manage its affairs "on a full-time basis." See 13 C.F.R. § 124.104(a)(1)-(2). Absent written approval of the SBA, the President or Chief Executive Officer of the small business may not hold "outside employment or any other business interest . . . which conflicts with the management of the firm or hinders it in achieving the objectives of its business development plan." Id. Because Investor A is the only investor in Company A who can hold the position of President and Chief Executive Officer, he must manage Company A on a full-time basis. Given that he is fully occupied with the management of Company A, Investor A cannot simultaneously be the full-time manager in charge of day-to-day operations of PCS Co., or serve as the President or Chief Executive officer of PCS Co., examples of management positions referred to in the new de facto control guidelines set forth in the Fifth Memorandum. See Fifth Memorandum at ¶ 80. In light of the obstacle created by the

requirements of Section 8(a), we seek confirmation that the Commission will apply its newly established de facto control guidelines flexibly where, as in the example described above, a pre-existing small business such as Company A will be providing substantial managerial services to an applicant and managerial positions in the applicant will be filled by (i) non-controlling officers of the pre-existing small business(es) that are members of the control group, e.g., Company A, who are employees of the pre-existing entity and under the direct supervision of a qualifying investor in the control group who also controls the pre-existing entity; and (ii) qualifying investors in the control group, e.g., Investor B.

Such a flexible application of the Commission's new criteria for de facto control would be consistent with the Commission's intent that, under a totality of circumstances standard, designated entities must in fact be controlled by qualifying individuals. The Commission has not changed its established view that de facto control is a question that is "inherently factual and therefore will require case-by-case determination." Fifth Memorandum ¶ 80. Thus, its newly established guidelines "are not necessarily dispositive of the issue of de facto control in all situations." *Id.* The fact that one index of control under these new criteria as set forth in ¶ 80 cannot be satisfied in these circumstances should not preclude satisfaction of the de facto control test when key managerial positions will be filled by qualifying investors and individuals who are directly supervised by qualifying investors. A flexible application of the Commission's guidelines seems especially appropriate to facilitate the participation of pre-existing small businesses that qualify under Section 8(a) of the Small Business Act. Furthermore, a flexible application would be sensitive to the fact that the de facto control guidelines were issued after many applicants had already filled senior managerial roles.

3. The Commission Will Not Adopt Any Presumptions That Women-Members of The Control Group Are Controlled By Their Spouses: The Commission has previously declined to adopt "any special rules or presumptions to determine whether women-owned applicants exercise independent control of their firms." *See* Fifth Report and Order, ¶ 189. We seek confirmation that the Commission will continue under the Fifth Memorandum not to apply any presumption to aggregate the interests of spouses for purposes of determining whether a woman exercises actual control of the applicant, and that any presumptions concerning spousal interests remain limited to the financial attribution context. *See* Fifth Report and Order at ¶ 212.

4. Pledges of Stock To Lenders or Equipment Vendors As Collateral in The Event of Default Would Not Be Attributed to The Applicant Or Qualify As a Transfer of Control: The Commission's rules, as modified by the Fifth Memorandum, "grant designated entities, particularly minority and women-owned applicants, additional flexibility in how they raise capital and structure their businesses." See Fifth Memorandum ¶ 4. These rules are designed to address the substantial barriers facing minorities seeking to raise money to compete effectively in capital intensive industries, such as telecommunications. See, e.g., Fifth Report and Order ¶ 100. We seek clarification that, consistently with these principles, the Commission will allow small businesses owned and controlled by minorities and/or women the flexibility to offer their lenders security in return for loans to the designated entities. In particular, we seek clarification that an applicant may pledge stock to its lenders and equipment vendors as collateral in the event the applicant defaults on its payments, as the Commission has traditionally permitted in the case of broadcast, cellular, and other licensees. Such a pledge would be made subject to the requirements that (i) the applicant retains voting rights in the stock prior to any default, and (ii) upon a foreclosure resulting from default or a reasonable time thereafter, the creditor must sell a controlling majority of the pledged stock to another small business owned and controlled by minorities and/or women. We seek further clarification that such stock pledges would not be attributed to the applicant or be treated as a transfer of control.

We believe this approach is consistent with the Commission's intent to strike a careful balance between facilitating the raising of capital by small minority-owned firms while ensuring that qualified individuals retain ownership and control of the applicant. See Minority Ownership in Broadcasting, 99 F.C.C.2d 1249, 1254 (1985); see generally S. Sewall, Assignments and Transfers of Control of FCC Authorizations Under Section 310(d) of the Communications Act of 1934, 43 Federal Communications Law Journal 277, at 337 (1991). Unlike stock options or other ownership rights that could potentially allow the holder to exercise actual ownership or control of the entity, the stock pledge arrangement contemplated above would not grant any control or ownership rights to the holder of the pledge other than the right to transfer ownership to another qualified licensee -- a right that matures only upon a default. We believe the strict limitations placed on this type of collateral, and the established commercial practice of giving such collateral to major lenders or suppliers, clearly distinguish this practice from the type of ownership rights that

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were contemplated by the Commission's full dilution and transfer of control rules. See Fifth Memorandum at ¶¶ 93-96, 123-127.

We thank you for your time and would appreciate your clarification of these issues as quickly as possible.

Sincerely,

A handwritten signature in cursive script that reads "William T. Lake". The signature is written in dark ink and is positioned above the printed name.

William T. Lake

cc: Andrew Sinwell  
Office of Plans and Policy